

THE CHALLENGES FOR MEDIUM- SIZED BUSINESSES IN MALAYSIA

Think Ahead

About the series



Medium-sized businesses play a fundamental role in global supply chains, yet many of them are running on legacy systems and processes, facing long-term underinvestment in skills and technologies and have a very strong case for change that crystallised after the outbreak of the Covid-19 pandemic. Neglecting their specific needs could cause considerable damage to economies in the medium term. This is clearly illustrated by the case of Malaysia, where there are many opportunities that need to be seized in the post-Covid period.

ACCA is presenting a series of thought-leadership pieces to support those working in medium-sized firms. Our introductory report, *The Challenges for Medium-Sized Businesses Post Covid-19*, is available on [ACCA Professional Insights website](#) or via the ACCA Insights app.

Time to revise the definition to enable growth?

In Malaysia, medium-sized businesses (MSBs) are a core part of the economy, according to the Malaysia External Trade Development Corporation (MATRADE), mid-tier businesses represent 30% of that country's total gross domestic product and employ 22% of its total workforce, and the government has a number of programmes targeted at aiding small and medium-sized enterprises (SMEs) to increase exports and strengthen their processes, as well as to digitise and automate (refer to a list of programmes in the box below).

Some programmes and initiatives targeted to support SMEs in Malaysia:

- High impact initiatives to drive export in SME sector by MATRADE
- Mid-tier companies development programme by MATRADE
- SME Digitalisation support programme with grants available by Malaysia Digital Economy Corporation
- SME Technology Transformation Fund (STTF) by Ministry of Finance of Malaysia and SME Bank of Malaysia

In practice, when defining what constitutes an MSB, the upper limit for company turnover is set quite low, leading some to argue that the 'true' medium-sized company is abandoned at a crucial stage in its development.

'We think that it is time to revise the definition of medium-size companies', says Datuk William Ng, chairman of SAMENTA, the Small and Medium Enterprises Association for Malaysian SMEs. 'Any manufacturer exceeding RM 50 million¹ would fall outside of the purview of our government intervention programmes, which I think is way too low'.

Ng argues that existing support schemes miss a crucial stage in medium-sized businesses' development – the very point at which support could be most beneficial. He says:

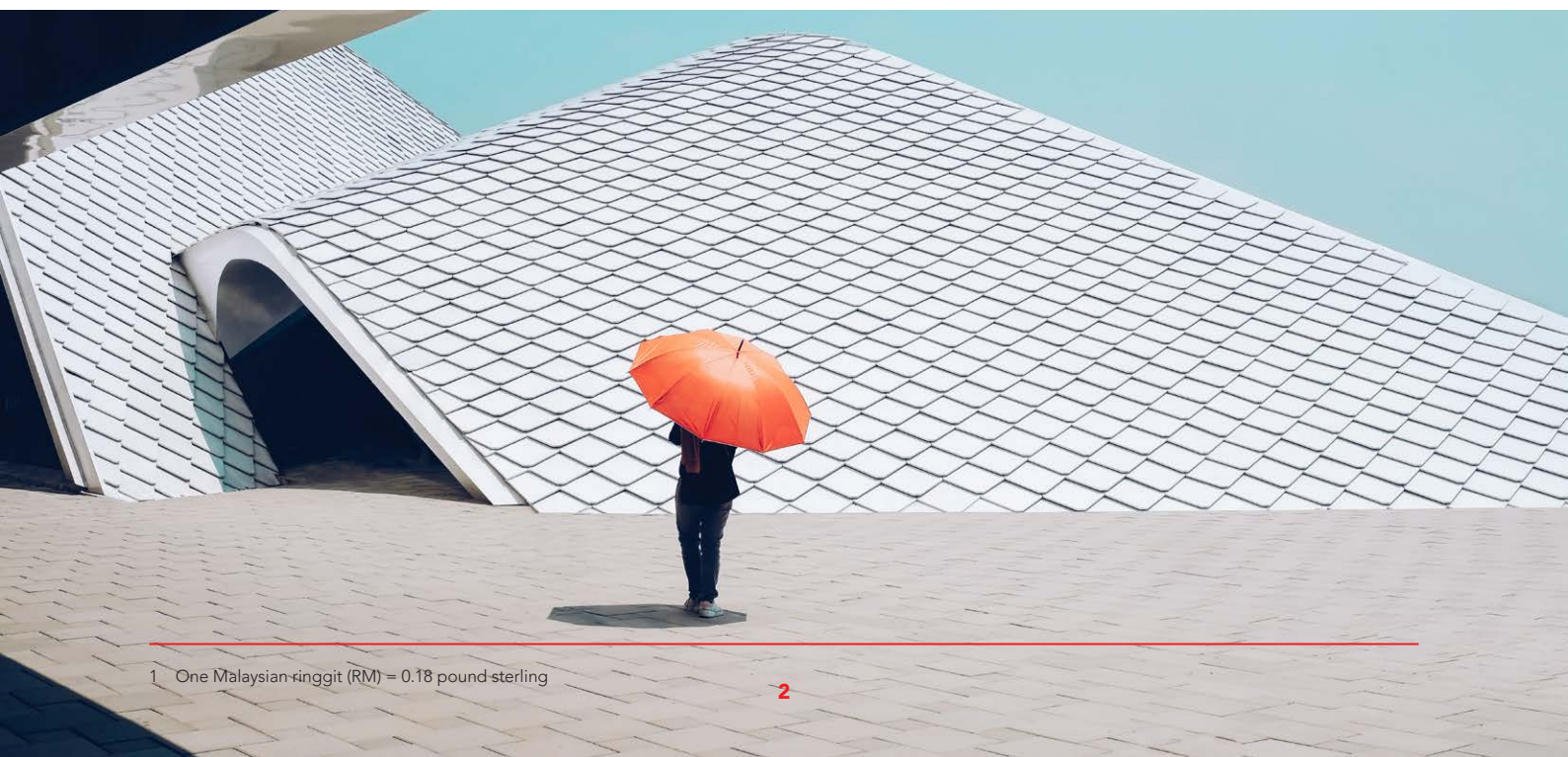
'Many entrepreneur-led SMEs fail in that transition to being a larger company – they might have tried to expand the business a little bit and then decide it is not such a great idea and scale back down'.

This inflection point is where MSBs encounter multiple obstacles to growth. People are a major issue: an expanding firm will need to set up an accounts department for the first time, and this means it has to compete for staff with bigger organisations. Many SMEs use free or subscription software and will also need to upgrade to more sophisticated and expensive IT systems. These costs begin to eat into margins.

'Most SMEs can survive on a tiny margin because of their cost structure, but as you grow bigger you hire more people and you put in more governance, [and] all this costs money', says Ng. 'All of a sudden the margin that you're happy with can no longer support you as [a] mid-market company'.

MSBs also face a knowledge gap: there is still a shortage of vendors targeting the sector, and owners lack the knowledge and expertise to maximise their product's appeal to a specific target market move up to a themed market.

'The International Trade Ministry as well as the Entrepreneurship Development Ministry have some good programmes, but the issue here is a general mistrust, or should I say misunderstanding, of what the government can do', says Ng. 'They are not reaching enough SMEs'.



¹ One Malaysian ringgit (RM) = 0.18 pound sterling

Ng is also concerned that Covid-19 has shifted SMEs' focus towards survival instead of growth. At the same time, the pandemic has also created a new breed of 'gig economy' homeworkers and online entrepreneurs. 'It's going to be very interesting seeing how they continue their businesses post Covid-19. Are they going to be changing into the next batch of SMEs?' he says. 'My other concern is the dynamics between the major online marketplaces and the small traders that are flooding them – the concern is the semi-monopoly of these marketplaces and what it means for local domestic retail businesses moving forward'.

Regulatory support required

Another area of concern for growing MSBs is government regulation: small businesses generally complain about 'red tape' but regulation can also provide valuable protection for growing companies.

Guard My Ride (GMR) provides an extended warranty service for used cars in Malaysia: and, according to founder and CEO Jonathan Tham, its presence in the market has not only increased sales but also raised standards in the used car sector. Yet he faces a lot of unregulated competition:

'We are the only company in Malaysia right now that is properly insured and regulated by an insurance company', he says. 'But there are other companies scamming consumers: following our business model but offering better coverage, cheaper rates and ridiculous terms and conditions, just to scam people of a few hundred ringgit. Last year alone, four of these companies just shut down shop. And the government isn't doing anything'.

GMR's ambition is to build an ecosystem of high quality services around its core warranty offering. For example, before the pandemic it was developing an app to help drivers maintain their cars properly and reduce breakdowns. Tham says the lack of government support for the sector is a missed opportunity:

'The automobile industry is the second largest contributor to the economy and the government needs to support any company that is involved in this industry, whether it be [in] the sales of cars, spare parts and even our own company', he says.

Tham says his company, although employing only 26 people, has not only helped dealers sell more cars by giving consumers peace of mind, but has driven up quality and innovation across the industry.

'We are one of the few countries in the world where BMW gives a five-year warranty and where for most continental brands the minimum warranty period is four years rather than two', he says. 'And this is because of our company'.

Covid-19 has hit the company hard but has also been a catalyst for developing the business model. GMR CEO Jonathan Tham says:

'This pandemic has taught us a lesson, you know, that we just can't rely on one channel of business, because presently 99% of our business comes from the dealer channel'.

Tham says his priority has been to maintain the team, trying to give them small assignments and get them to come up with ideas for process improvements.

'I've been asking them to think about how we could improve our back-end service operations on sales and marketing, once we're able to open for business', says Tham. When the situation stabilises, the plan is to get expansion plans back on track, with joint ventures in adjacent markets with similar characteristics: 'Indonesia, and Thailand have very similar ecosystems and culture to Malaysia, so we understand the risks involved', says Tham.



Understanding the ecosystem is key

Understanding the business ecosystem in which MSBs operate is key to helping them prosper.

GSH Precision Technology Sdn Bhd was established 20 years ago in Penang. The company develops high-end machining components, installation of robotic arm, system integration and other customised equipment to multinationals, both in Malaysia and globally. As such, it is one of many mid-tier companies that form a vital part of the supply chain for some of the world's biggest multinational corporations (MNCs).

'We are embedded as part of the ecosystem supporting multinational corporations', says Business & Corporate Director Prof J. Philip Vincent. 'There are a lot of opportunities that multinational corporations have contributed to the Malaysian economy in terms developing and cultivating entrepreneurs and SMEs'.

At the human resource level, competition can be fierce, both from other MSBs and clients.

'We are hungry for a lot of engineers and skilled workers in Penang, so what the Industry Captains have done is set up the Penang Skills Development Centre, which has cushioned a lot of talent workforce issues for local SMEs', says JP Vincent. 'I sent my engineers and technicians for further training as well as reskilling so that they could acquire latest technologies in production process'.

This is vital because part of GSH Precision's response to Covid-19 was to build on government support to restructure its operations using technology:

'During lock down, the government came up with a solution of allowing factories to have 20% working from home and 80% working at the factory', says JP Vincent. 'So we accepted it, but along our journey we found that this would be a continuous issue for us'.

The company has invested in software to digitalise our production systems and allow remote monitoring, and staff have had to adapt to home working seamlessly. 'This has been difficult for our staff to get used to it due to new culture, but after 18 months all of them are professionals in handling day-to-day operations on their PCs', says JP Vincent. 'This is going to be our culture now and we have to learn to live with it'.

As a result of software implementation, the company reduced the operating costs by 15%. And, while this transition built on pre-Covid government initiatives to encourage SMEs to adopt digital transformation, the pandemic proved to be the catalyst that has impelled a lot of SMEs to move much faster in that direction.

The digital transition has also required investment in upgrading production equipment to be compatible with Industry 4.0 and the associated increased use of data. The next step will be automisation and artificial intelligence (AI): GSH Precision Technology Sdn Bhd is growing and focus on incorporating new technology to reduce cost and increase efficiency with continuous employee training programs to keep them abreast with the MNCs needs'.

It's expensive, but only keeping up with the demands of customers will enable GSH Precision Technology Sdn Bhd to execute its expansion plans: 'Yes, we are expanding, and we want to compete to stay relevant in business', says JP Vincent, 'and we have plans that we are embarking on right now, providing higher-end services for the semiconductor and wafer [semiconductor material] industry'.

Conclusion

As the economy emerges from Covid-19, Malaysia's MSBs are poised to make the transition from survival to recovery, and then to growth. The inflection points when moving from the small to the medium bring multiple challenges for recruiting and retaining talent, updating processes and sourcing appropriate IT applications. Navigating to growth will require medium-sized companies to transition prudently from current methods to operating at scale in a digital world.

Government support, proportionate regulatory frameworks protecting medium-sized businesses and enabling their growth, and supportive business ecosystems are essential in helping this important segment of economy to make this transition. Understanding the specific needs of the medium-sized enterprise sector is crucial in navigating the path to recovery and growth, and requires regular dialogue between the representatives of the sector, the government and support institutions.

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